



Consumer Federation of America

**STATEMENT OF DR. MARK COOPER
DIRECTOR OF RESEARCH**

THE FINANCIAL STATUS OF THE AIRLINE INDUSTRY

**COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION
UNITED STATES SENATE**

September 20, 2001

Mr. Chairman and Members of the Committee,

My name is Mark Cooper and I am Director of Research for the Consumer Federation of America¹. I am accompanied today by the Consumer Federation's Director of Insurance, J. Robert Hunter, who will be available to answer any questions that may arise regarding the insurance implications of this issue.

Having testified before the Congress and other federal agencies about 150 times, I am well aware of the routine statements of appreciation that witnesses provide when they thank the Committee for the opportunity to testify. This is a very special hearing, in light of the tragic events of last week, so in thanking you for the opportunity to express the views of the Consumer Federation of America today, let me point out that it is proceedings such as this, in which the committee will hear differing points of view, that are a significant part of the freedom we are fighting for. As a democratic society we are unified in our purpose to combat terrorism. We should be equally committed to allowing open dialogue as to how best to achieve that purpose, especially when it comes to using public funds to support commercial enterprises. This is, indeed, a rare opportunity that I truly appreciate.

¹ The Consumer Federation of America is a non-profit association of more than 280 organizations that, since 1968, has sought to advance the consumer interest through advocacy and education.

Although it is unlikely that Congress will consider propping up the many businesses that may go bankrupt in the months ahead as a result of the slowing economy and the tragic events of the past week, it is appropriate to consider some financial support for the airline industry. We should ensure that the industry does not collapse because of its unique role as a part of the essential infrastructure of the 21st century economy and society and the severe impact that the attack has had on it.

Airlines may need a limited infusion of cash to keep them afloat, but we should also inject rationality into the way this industry does business. In addition to ensuring a more secure air travel network, it is absolutely appropriate for Congress to require fairer competition, better service, and more effective consumer protection in exchange for assistance to commercial operators. The airline industry was falling seriously short in these crucial areas before the attack.

Moreover, it would be a mistake to include hastily drafted industry proposals for legal indemnification and an antitrust exemption as part of this financial assistance package. There will be adequate time in the next few weeks to thoroughly discuss the implications of these longer-term proposals, parts of which may be ill-advised and harmful to consumers, and to prepare a legislative response if necessary.

Recognizing that airspace is a limited resource, more precious now that security measures are likely to make it scarcer, we should not waste it, nor should we allow it to be monopolized by a few large carriers. Our goal should be to preserve the value and convenience of our transportation system as best as possible, within the confines of the new dictates of security. Once procedures to promote security are in place, we must find ways to ensure that competition fairly allocates resources within the industry, such as routes, landing slots and airport gate space. This will be a challenging task because of reduced capacity.

Keeping The Air Travel System Running In The Short Term

In the short term, we are not opposed to limited financial assistance to the industry, as long as it is based on a fair and careful accounting of the industry's short-term financial obligations, their losses and the extent of government responsibility for these losses. For example, it is reasonable to consider providing compensation for costs related to the shut-

down of airline operations last week, as the FAA mandated this interruption because of national security concerns.

The goal should be to keep airlines out of bankruptcy as long as a national emergency exists, but that does not mean writing them a blank check. Bond covenants have financial coverage ratio requirements and leasing arrangements identify minimum payments that must be met to avoid technical bankruptcy. That is the level of financial commitment that Congress should make. Airline management should not be excused from the obligation to efficiently adjust their operations to a new marketplace.

Much of the cost of this adjustment is being shifted to the public through lay-offs, the brunt of which will be borne first by the affected employees and then by the treasury for unemployment and other benefits. To the extent that there is a permanent downsizing in the industry, funds should be made available to ease the transition for air industry workers as well.

Creating a Survivable Transportation Network in the Longer Term

In the longer term, building a survivable transportation network requires redundancy and diversity of transportation options, as well as air travel decentralization. Here are some ideas that should be considered and debated.

First, we should improve ground transportation, particularly high-speed rail in high-density air corridors. This could relieve a substantial part of the load in the most densely traveled routes without imposing significant indirect costs (increased travel time) on the public. It would also ease runway overcrowding at some airports. It would probably require the airlines to cut back on some of their most densely traveled and profitable routes for the sake of the public interest.

Commercial operations that require plane changes by driving traffic through hub and spoke networks make economic sense for the air carriers, but they are heavy users of very scarce resources – take offs, landings and air traffic control. For consumers, however, the hub and spoke system has led to domination of routes in some regions by a single carrier, resulting in higher ticket prices. These networks also impose a transaction cost on the public that may

increase substantially – boarding time. Concentrating traffic is profitable for the airlines and it may even be efficient, but it may not be in the public interest, given the new traveling reality.

It may be necessary to separate different types of air traffic because they pose different security risks. Screening passengers is different from screening freight. General aviation, because it is not public transportation, can be required to have lower priority. We may have to allocate our scarcest resource – daylight hours at airports nearest to population centers – to moving people and relegate other types of traffic to off peak hours and more distant airports.

We may also have to rethink expansions of airport capacity. Rather than adding runways at already overcrowded airports, it may be preferable to add airports handling different types of traffic.

Consumer Protection

In addition to securing the safety of the traveling public, their rights as consumers should also be protected. If consumers are not treated fairly, they will obviously be less likely to fly, especially given the security concerns they may already have. It will also be harder to gain the long-term public support needed to build the transportation network we need.

For many years now, airlines have been unable to deliver decent, on-time service to the public. A variety of causes have been cited – over-scheduling, inadequate airport capacity, antiquated air traffic control. This problem will get much worse since airline capacity will now be reduced by security concerns. We never want a plane to rush or to take off before it is secure and safe to do so, but the public deserves to be given honest and reasonable information about when planes will take off and land.

The public should pay only once for ensuring the physical safety of passengers and the financial viability of the air travel system. Airport and air travel security are national security matters that should be the direct responsibility of government (federal and local) security forces, not private subcontractors of airlines and airports. Increasing governmental outlays for security can be offset by reduced private expenditures. Lay-offs shift costs to the public; airlines do not need to be compensated a second time.

If billions are to be spent to directly support the airlines, then some agreement on ticket pricing must be reached. This is especially necessary in light of the fact that the already inadequate level of competition in the industry is likely to be diminished by the reduction in system capacity.

Providing an antitrust exemption for allocating slots and routes, as has been suggested by some airlines, raises a host of serious concerns that must be considered at length. Larger airlines would likely attempt to use such an exemption to gain access to the most profitable routes and facilities. The survival of individual airlines will be determined by whether they have access to the most valuable air space and to airports near population centers during daylight hours. If we are going to preserve a competitive and convenient air travel industry, these finite public assets must be managed properly and shared among airlines, regardless of size.

Having the government get involved in these issues may be a step back from the philosophy of “let the marketplace decide,” but asking the American taxpayer to pay billions to prop up airlines is the first step in that direction. In a general way, for the past several decades, we have neglected our infrastructure. The current crisis may refocus the nation’s attention on this important issue. Making long-term decisions in a crisis mode does not always lead to the best choices. Having an open and thoughtful debate about the best policies in pursuit of new national goals, while spending the public’s money, is the cornerstone of our democracy and likely to produce a much more effective long-term result.

Thank you for the opportunity to offer these comments.